

# Joint Economic Committee WEEKLY ECONOMIC DIGEST

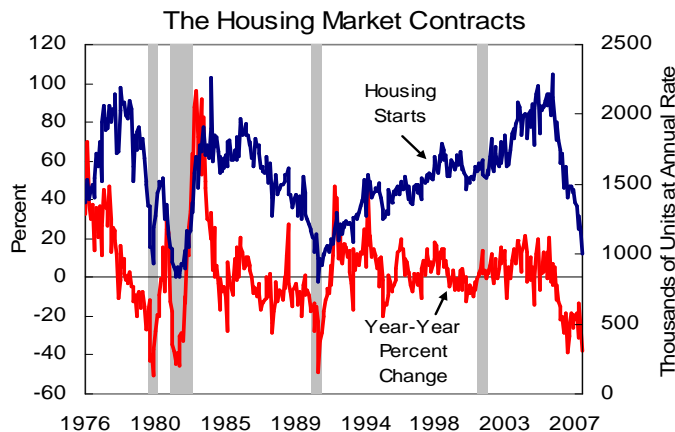
Senator Charles E. Schumer, Chairman  
Congresswoman Carolyn B. Maloney, Vice Chair

January 29, 2008

## ECONOMIC NEWS

### Economic Woes in Housing and Employment

**Housing market continues to contract.** Recent releases of home sales data show that weakness in the housing market is persisting. This week's release from the Census Bureau showed that seasonally adjusted new home sales are down 4.7% from last month and down 40.7% from December 2006. Additionally, the months' supply of new homes is up to 9.6 months, compared with 6.2 months in December 2006. Previously, the Census Bureau released data on housing starts showing a marked deterioration in new construction (see chart). Last month's decline in the number of new housing starts is similar to what was experienced during the recessions in the 1980s.



Note: The gray areas indicate periods of recession as defined by the National Bureau of Economic Research.

Sources: U.S. Department of Commerce and National Bureau of Economic Research.

Similarly, data from the National Association of Realtors (NAR) released last week showed seasonally adjusted sales 2.2% lower than in November and 22% lower than sales in December 2006. Moreover, sales of existing homes in December declined in all regions of the U.S., including the West, while November's decline was limited to the Northeast and the South. Additionally, the median sale price for existing U.S. homes declined 1.4% between 2006 and 2007, the first decline since the NAR started tracking these data in 1968.

**December employment reports were bleak.** The December employment report, released earlier this month by the Bureau of Labor Statistics, showed that the unemployment rate rose to 5.0% in December, an increase of 0.6% from last year, and a jump of 0.3% from last month. Additionally, the number of jobs in the private sector declined by 0.13% at an annual rate. Moreover, the employment-population ratio declined by 0.7% since November. Last week's initial jobless claims declined by 1,000, leaving the number of newly unemployed virtually unchanged.

## IN FOCUS

### Averting Recession

Last Tuesday the Federal Reserve Open Market Committee (FOMC) took dramatic policy action, cutting the target Federal Funds rate by 3/4 percent. The rate cut was taken before Wednesday's regularly scheduled FOMC meeting and is the single largest rate cut in 26 years. The Fed Funds rate now stands at 3.5 percent, down from 5.25 percent in August. Many anticipate that the FOMC will make an additional rate reduction when it meets this Wednesday.

Some view last week's rate cut as a measure to prevent a fear-driven rout in U.S. equity markets, which seemed likely after declines on foreign exchanges. While events in stock markets may have contributed to the timing of the Fed's announcement, they do not explain the decision to cut the rate or the size of the cut. The Fed's mission is not to protect the value of financial assets or financial market participants.

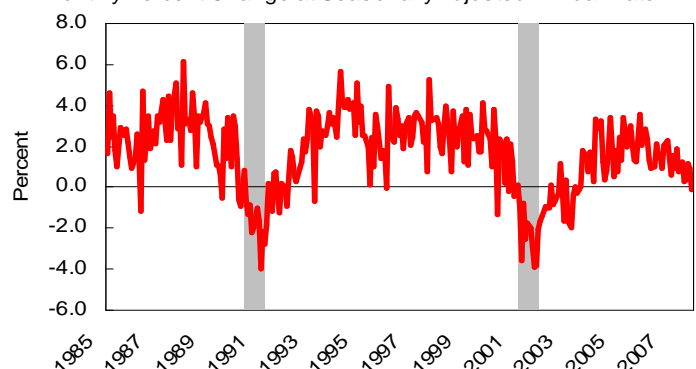
To the contrary, the FOMC explained that it was taking action because of the continuing decline in the overall performance of the real, non-financial economy. Declining employment and output growth motivated the rate cuts, and these developments are attributable only in part to events in the credit markets.

To be sure, problems in credit markets are clearly visible in economic statistics. Outstanding asset backed commercial paper, for example, has contracted by about one-third from its August value. (See Snapshot) But problems in the real

*Continued on reverse...*

### Private Job Growth Negative for First Time Since Jul '03

Monthly Percent Change at Seasonally Adjusted Annual Rate



Note: The gray area indicates a period of recession as defined by the National Bureau of Economic Research.

Sources: U.S. Department of Labor and National Bureau of Economic Research.

# Joint Economic Committee WEEKLY ECONOMIC DIGEST

## THE WEEK AHEAD

DAY	RELEASE
Tuesday, Jan 29	Consumer Confidence (December 2007)
Wednesday, Jan 30	GDP Advance (Fourth Quarter 2007) Federal Open Market Committee (FOMC) Policy Statement
Thursday, Jan 31	Employment Cost Index (Fourth Quarter 2007) Core PCE Inflation (December 2007)
Friday, Feb 1	The Employment Situation (January 2008)

**Friday  
Feb 1st:  
JEC Hearing on  
Employment  
Situation with  
BLS  
Commissioner  
Keith Hall**

## IN FOCUS (Continued)

economy are also apparent, and extend well beyond problems in housing, as can be seen in the data on nonfarm private employment. (See chart on previous page).

Although rate cuts will help to stimulate demand, they are unlikely to be enough to forestall a significant downturn. Monetary policy works through intermediaries, such as commercial banks and mortgage lenders, and it can take well over a year to be fully felt. Moreover, when the economy is in decline, households and firms become more cautious and spend less, and this can counteract the effects of interest rate changes.

This explains why fiscal stimulus is also on the agenda. A well-crafted program that increases spending can rapidly generate a predictable boost to the economy. However, the “multiplier” or “bang for the buck” of potential stimulus options varies significantly.

It is generally recognized that transfers to income-constrained or credit-constrained households are likely to be spent rapidly. So, for example, increased unemployment insurance payments or food stamp distributions are very likely to produce proportionally large, immediate impacts. Tax rebates, especially when targeted to low- and middle-income households, are likely to have large effects. On the other hand, tax cuts designed to stimulate business investment have smaller impacts, because investment decisions also depend on expected demand and other factors. (For a ranking of stimulus options see [http://www.cbo.gov/ftpdocs/89xx/doc8916/01-15-Econ\\_Stimulus.pdf](http://www.cbo.gov/ftpdocs/89xx/doc8916/01-15-Econ_Stimulus.pdf))

The overall effect of a fiscal stimulus depends on its total size, as well as the “bang for the buck” of its elements. The stimulus packages currently under consideration are equal to about one percent of GDP. If the adopted package has carefully chosen elements, which might result in an aggregate multiplier effect roughly equal to one, then it may add about one percent to GDP. This would give the economy a decent boost.

If a truly big downturn is under way, however, a one percent stimulus may not be enough to prevent rising unemployment and declining growth. In that unfortunate case, follow-on stimulus may need to be considered.

## SNAPSHOT

